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SUBJECT: DEVELOPMENT IMPACT OF STAN

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1. Summary: Still gripped with the immediate concerns of disaster relief, GOG officials have not yet tallied the economic costs of Tropical Storm Stan and the accompanying rains that drenched more than one third of Guatemala's territory in the first two weeks of October. Some estimates have put the damage between USD 2-3 billion, equivalent to around 10 percent of GDP. Whatever the numbers, the effects on human life, property and economic infrastructure are devastating. According to the GOG, an estimated 30 percent of Guatemala's 13 million people suffered with loss of life, property or access to basic services. About seven hundred have been confirmed killed with close to a thousand more still missing. Disaster related disease and impoverishment are expected to claim even more lives. As the GOG moves from relief to reconstruction, the impact on Guatemala's development will become clearer. The storm was a tremendous blow to recent progress in the GOG's development plan, including ambitious efforts to turn around the long-stagnant rural economy. End summary.

The Economic Damage: Threat to Rural Survival

2. Floods and landslides devastated the southern coast and the heavily populated and impoverished Central and Western Highlands. The medium to long-term effects on Guatemala's marginal rural economy may be as devastating as the initial impact. Economic activity, particularly in the highlands, will suffer from the loss of key infrastructure including bridges, roads, telecommunications and energy distribution in the short to medium term.

3. Much of the population of the areas most affected already live day-to-day, depending on subsistence crops and informal economic activity for their livelihood. It is unclear how the more than 150,000 people made homeless by the storm - some just now returning from temporary shelters - will survive the coming months. The Vice Ministry for Housing has requested USD 125 million for housing replacement and repair assistance. The potential benefits of CAFTA along with the Berger Administration's ambitious development plans are at risk as key growth sectors such as non-traditional exports, agriculture, tourism and transportation services are severely damaged by the storm. An ECLAC-led team is currently developing a formal damage assessment, to be completed November 8, which will serve as a basis for the government's reconstruction plans.

The Macro Picture: Hitting Where it Hurts Most

4. On paper, Guatemala's macro-economic outlook will remain stable as economic losses, primarily in the agricultural and distribution sectors, will likely be somewhat offset by increased spending on infrastructure and rebuilding efforts. With the help of anticipated international assistance, the GOG, which had been on track to significantly outperform fiscal deficit projections, should be able to increase spending on disaster relief and still meet initial deficit projections of 1.8 percent of GDP. However, Guatemala suffers from the second worst income distribution in the hemisphere and is the most densely rural country in the region. With most people in rural areas (where storm damage was worst) getting by on annual per capita income of less than USD 1,000, even a temporary loss of income may make life in some affected areas unsustainable.

Infrastructure: People and Services Inaccessible

5. More than 25 percent of the country's paved roads and 50 percent of dirt roads were damaged or made inaccessible. Seventeen bridges collapsed, leaving large parts of Guatemala's rugged countryside unreachable. Some particularly remote areas are still beyond the reach of aid workers. Ministry of Infrastructure initial estimates of the costs of repairing roads and bridges are over USD 350 million. The energy sector suffered heavily in both generation and

distribution. Hydro generators alone suffered well over USD 2 million in losses, some southern coast thermal generators were flooded, and line damage repairs in the distribution network are ongoing. Most of the heavily populated western portion of the country was left without power immediately following the storm and international grid links to Salvador were cut off. It is too early to tell the extent of ongoing economic losses as a result of key infrastructure damage. The impact of this damage will undoubtedly increase initial losses in other sectors such as agriculture, tourism and transportation as the country struggles to rebuild.

Agriculture: Subsistence Crops Threatened

16. The Ministry of Agriculture's initial estimates put losses at over USD 250 million. This includes substantial damage to major employers such as sugar cane, which lost approximately 10 percent of the current harvest, coffee, which is reporting some USD 14 million in losses, and shrimp and sesame, both reporting total losses due to the sensitivity of their product to flooding. Perhaps most worrying but least quantifiable economically is the damage to subsistence crops, on which Guatemala's most marginal populations rely. Many rural agricultural workers depend on their small corn harvest to feed them in between seasonal work on the major cash crops such as sugar and coffee. With less to live on now and anticipated losses in seasonal employment, Guatemala's rural populations will continue to suffer severe hardship from the storm.

Tourism: Growth Industry Hit Hard

17. The Guatemalan Tourism Institute (Inguat) estimates a drop of 100,000 tourists this year at a cost of USD 80 million to the industry. Particularly damaging will be losses around Lake Atitlan. This already poor, densely rural area of Solola not only suffered some of the most dramatic damage from the storm, including the deadly burying of the village of Panabaj, but the economy depends on many micro-businesses that cater entirely to tourists. It is unclear how people will adjust even after roads and access are restored, as tourism will likely suffer for years to come. Losses to the bigger tourism businesses in the lakeside town of Panajachel alone are costing over USD 250,000 per week.

Threat to Medium and Long Term Development

18. The Berger administration's ambitious development program was based on several key initiatives aimed at bringing the long-ignored rural populations into the economic fold. An aggressive international free-trade agenda including CAFTA promotion and trade capacity building, along with domestic efforts to shift government spending toward education and healthcare sought to better prepare the average Guatemalan to participate and compete in an open economy. These efforts were combined with localized projects to use infrastructure and education to link up small rural producers to the global market. The non-traditional export chamber (Agexpront) along with the Ministry of Economy had been having some success with local artisans and farmers of specialty crops such as snow peas, specialty coffee and winter vegetables. Efforts at improving education, expanding access to credit, reducing bureaucracy and otherwise facilitating small business development showed great promise for increasing formal sector participation in the rural highlands. Inguat had been aggressively pushing sector development in some of the hard-hit areas such as Solola, Quetzaltenango, San Marcos and the southern coast.

19. The ambitious goals of the development plan "Vamos Guatemala" have not changed, but the economic climate and the government's capacity to implement the plan suffered a potentially lethal blow by Stan. With GOG and international energy and resources focused on helping people survive the immediate effects, their ability to continue to promote development is in question. There is a potential for rural economic collapse far worse than that which followed Hurricane Mitch and the coffee crisis. Those crises dramatically set back rural development, worsening all major poverty indices, and drove a surge in migration to the slums of Guatemala City and to the United States.

Rural Destabilization and Migration

10. Stan was a blow to the part of Guatemala that could least absorb it. The GOG's rural development plan not only lost momentum but leapt backwards in some of the most desperately poor areas of the hemisphere. It is unclear how the resource-strapped government will be able to rebuild what was lost and simultaneously continue to develop the human and physical resources needed to put rural Guatemala on a sustainable path of job creation. It is also unclear what impact the disaster

will have on the political climate and the prospects of a like-minded government succeeding the Berger administration to provide much-needed policy continuity.

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